Legacy



# Annual Report 1989

Legacy Petroleum Ltd.

## CORPORATE PROFILE

**Date Incorporated**
October 14, 1970

**Incorporated In**
Province of Alberta

**Date Continued**
February 11, 1983

**Year End**
31 May

**Predecessor Companies**
Francis Creek Mines Ltd. (NPL)
Oct. 14, 1970 - Jun.14, 1971
Frances Creek Mines Ltd. (NPL)
Jun. 14, 1971 - Sept. 9, 1975
Cal-West Petroleums Ltd. (NPL)
Sept. 9, 1975 - May 24, 1985

**Head Office**
#530, 777 - 8th Avenue S.W.
Calgary, Alberta T2P 3R5
(403) 264-4254

**Field Operations**
Halkirk Gas Plant
Phone & Fax: (403) 884-2469

Castor Gas Plant
Phone & Fax: (403) 884-2554

**Wholly Owned Subsidiaries**
Legacy Oil and Gas Ltd.
Legacy Oil and Gas Inc.
Benchlands Oil and Gas Inc.
Harkor Developments Ltd.

**Partly Owned Subsidiaries**
363304 Alberta Ltd. (71.07% owned)

**Directors**
Murray F. Craig
William Y. Kennedy, LL.B
Carol A. Mossfeldt
A. Kenneth Mossfeldt

**Officers**
A. Kenneth Mossfeldt
President

Carol A. Mossfeldt
Vice-President, Administration

**Transfer and Registrar Agent**
Montreal Trust
411 - 8 Ave. S.W.
Calgary, Alberta T2P 1E7

**Auditor**
M. Jane McKinnon, C.A., B. Comm.
Calgary, Alberta

**Main Banking Connection**
Treasury Branches of Alberta
Calgary, Alberta

**Other Banking Connections**
Northwest Trust Company
Calgary, Alberta
First State Bank of Shelby
Shelby, Montana USA

**Stock Exchange Affiliation**
Alberta Stock Exchange
Calgary, Alberta

**Trading Symbol**
LCY-A

**Share Type Capitalization/ Issued and Outstanding**
Class "A" Voting Common Shares
unlimited - 3,433,958

Class "B" Non-Voting Common Shares
unlimited - nil

**Preferred Shares** - 500,000
250 Series #1 - Redeemed & Cancelled
22,000 Series #2 - As of 31 May 1989
19,000 outstanding
19 Series #3 - As of 31 May 1989
19 outstanding

**Printed By**
The Copy Cellar

## PRESIDENT'S MESSAGE

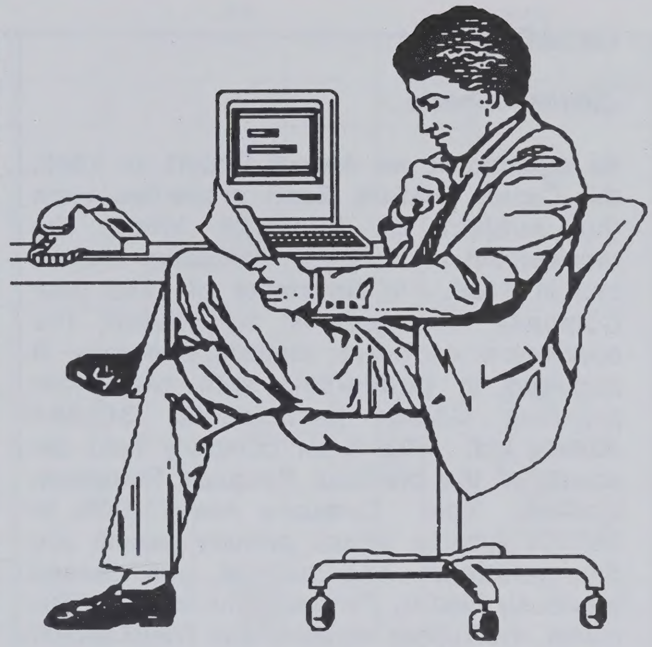
On behalf of your Board of Directors, I present the Annual Report of the Company containing the financial results for the year ended 31 May 1989. While the financial results in terms of cash flow are disappointing, the Company has been in the process of building a predominantly natural gas asset base from which it can grow and develop during the coming decade.

Undoubtedly, one of the single most significant changes that the non-renewable energy sector is facing in the immediate future is the emergence of natural gas as the primary fossil fuel for North America. With growing concern over world wide pollution, as well as the volatility of supply and demand particularly for North America, crude oil has during the 1980s lost some of its appeal. Along with the transition from crude oil to natural gas will come an increase in the price for suppliers -- an increase which for companies such as ours will be much welcomed, and immediately evident in the cash flows.

Your Company has substantial natural gas reserves as evidenced in engineering data prepared as of 01 August 1989 and contained on page seven of this Report. We are now actively seeking investor participation to develop these reserves to their maximum potential. With gas processing capacity of ten million cubic feet per day from our two plants strategically located in close proximity to the majority of our reserves, we view the Company as well positioned to move into the role of a significant supplier and producer of natural gas.

In keeping with the foregoing concept, we proceeded to increase working interests and acquire additional production in the Halkirk/Castor/Leahurst area of east central Alberta during the past fiscal year. While the Leahurst area purchase has not had a significant impact on cash flows from currently producing wells, the shut-in gas ready to be placed on production could have a beneficial impact prior to the end of the present fiscal year.

In addition to the development of the Company owned reserves, we are moving into the custom gas processing field. We are currently processing gas for one operator in the area and negotiations



are underway with a number of additional companies for the processing of their natural gas. Our current charge for gas processing is forty-two (42) cents per thousand cubic feet and as more contracts are executed it is anticipated that processing will also have an impact on cash flows during fiscal 1990.

Efforts to acquire additional producing properties during the past year could not be successfully concluded. Financing for even established production appears to be very limited from banks, as well as from the private sector. However, your Company will continue through the current year to look for additional reserves that are affordable.

In conclusion, the value of our shares rose sharply during the last quarter of fiscal 1989 and the first quarter of fiscal 1990. We appreciate the confidence that our Shareholders, past and present, have demonstrated through our share price and assure all Shareholders that we will endeavour to make your Company viable and financially sound through the coming year.

A. Kenneth Mossfeldt
President
on behalf of the Board of Directors

24 November 1989

## CANADA

### *Castor, Alberta*

As reported in our Annual Report for 1988, the Castor (Halkirk East) properties were the subject of litigation since the receivership of Pangaea Petroleum Limited late in 1986. in November of 1988 your Company successfully negotiated the conclusion of these matters, whereby it acquired in partnership with two other previous Castor participants, 363304 Alberta Ltd. This latter company held the assets of the previous Pangaea Petroleum Limited. Your Company has 71.07% in 363304 Alberta whose primary assets are the petroleum and natural gas leases previously held by Pangaea. In resolving this matter, the Topgas repayment to TransCanada which was the primary issue of legal proceedings was repaid in full by B.C. Bancorp and your company in partnership was responsible for outstanding lease rentals and taxes on the properties. We are pleased to report that as of the date of this report, only a small amount of rentals remain payable to the Crown, who had in turn reimbursed certain farmers in the area for lease rentals not previously paid by Pangaea. Taxes on these properties are currently being reduced on a monthly basis.

In November of 1988 production was recommenced at Castor. However, production problems coupled with low productivity of wells currently tied in, resulted in losses both for your Company and its partly owned subsidiary 363304 Alberta Ltd. Your Company is currently examining a number of avenues to remedy the problems at Castor. The results of these negotiations will be reported to shareholders as they are concluded.

The map on page four highlights your Company's holdings in the Castor (Halkirk East) area. The Reserves Report on page seven confirms that the Castor (Halkirk East) area has 563 MMCF of recoverable raw gas.

### *Halkirk, Alberta*

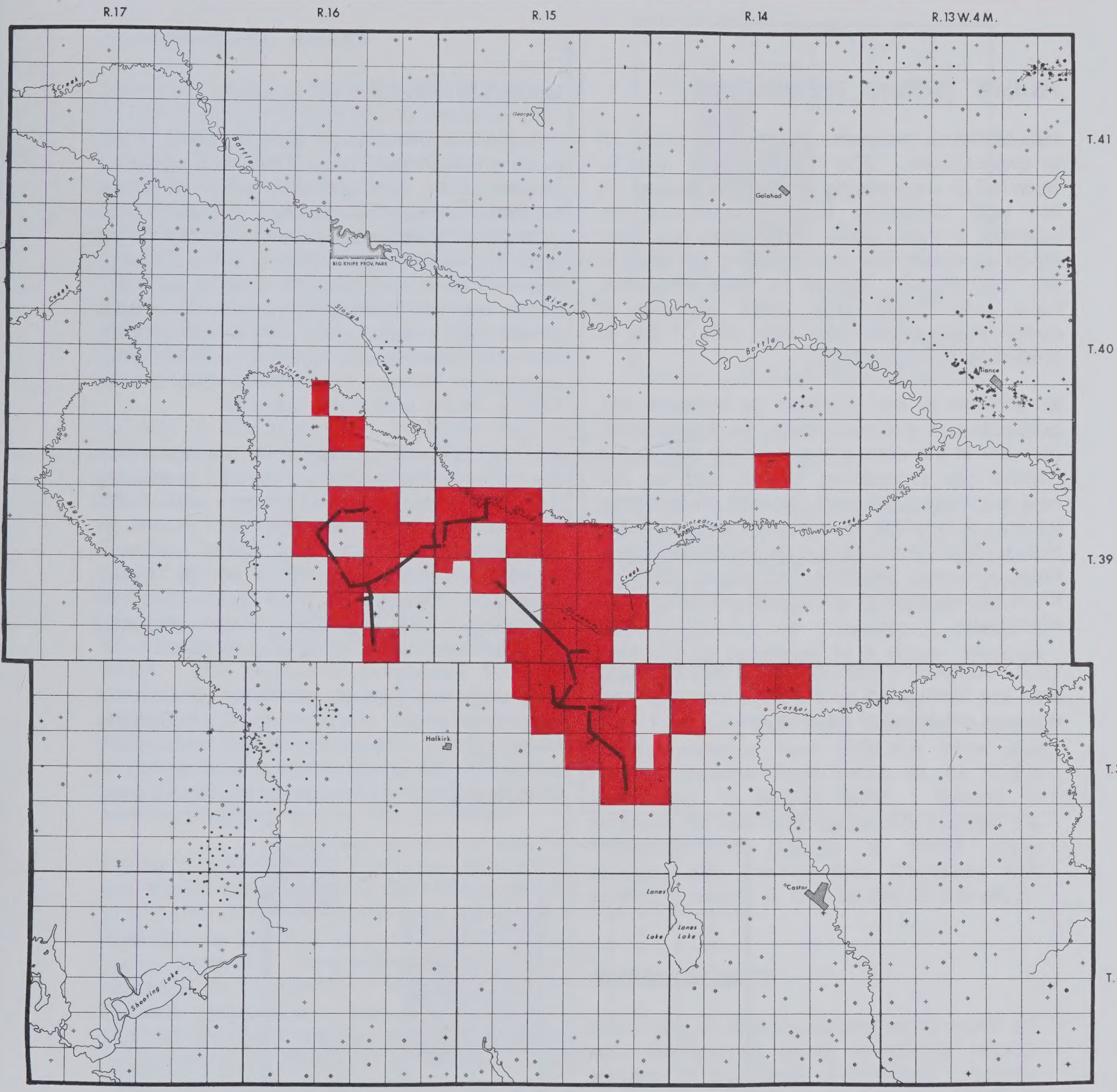
In last year's Annual Report, your Company noted a number of activities that were to occur over this fiscal year. The farmout to PanCanadian Petroleum in Township 39, Range 16 W4M resulted in a well being drilled. This well tested gas at 850 MCF/day from the Basal Quartz zone but PanCanadian considered the well noncommercial, and it was abandoned. Inasmuch as your Company has two Viking gas wells in this section, it was not prudent to complete this well. PanCanadian elected not to exercise its option to drill in Section 30, Township 39, Range 15 W4M.

In addition to the above, your Company had negotiated a seismic option with Erewhon on three sections. However, upon conclusion of the seismic activity, Erewhon elected not to exercise its option to drill on these leases.

It must be kept in mind that while neither of the above activities resulted in further dilling on our acreage, it does not necessarily indicate that these leases are unattractive for future development. The unprecedented volume of producing properties that came on the market in early 1989 has resulted in many companies re-thinking their objectives. The downturn in drilling which is now crippling the service industry has also had an impact on companies such as yours in negotiating farmouts which will result in drilling.

During the year your Company opted to try to improve production from currently producing wells, rather than financing additional drilling. The gas well in LSD 13, Section 14, Township 39, Range 16 W4M previously acquired from Resman, was perforated and reworked but needs additional evaluation prior to putting on production. As well, your Company did workovers on its well in LSD 16, Section 24, Township 39, Range 16 W4M which had encountered both oil and gas in 1986, and its oilwell in LSD 10, Section 21, Township 39, Range 15 W4M which has

(continued on page five)




*LEGEND*

- LEGACY INTEREST LEASES
- LEGACY OPERATED GAS PLANT
- GAS GATHERING FACILITIES

LEGACY PETROLEUM LTD.

RED WILLOW AREA

GASWELL
OILWELL
ABANDONED

| Scale: 1 100,000 | Date: JUNE 1, 1988 | By |
|---|---|---|

### *Halkirk, Alberta (continued)*

substantial oil reserves. Neither has produced to expectations. The results of the reworks were not as encouraging as had been hoped for, but your Company is still assessing the potential of these wells. Application has been made to obtain 320 acre spacing for Section 24, Township 39, Range 16 W4M where we have two Viking gas wells capable of commercial production but only 7-24 is producing at the moment.

In addition to our attempts to increase gas production at our own wells, an independent operator in the area tied-in a single well to the Halkirk gas processing facility, and we are now processing gas from this well on a custom basis. A number of other operators in the Halkirk North area have expressed interest in tieing into our facilities, but again many of these developments are based on favourable economics.

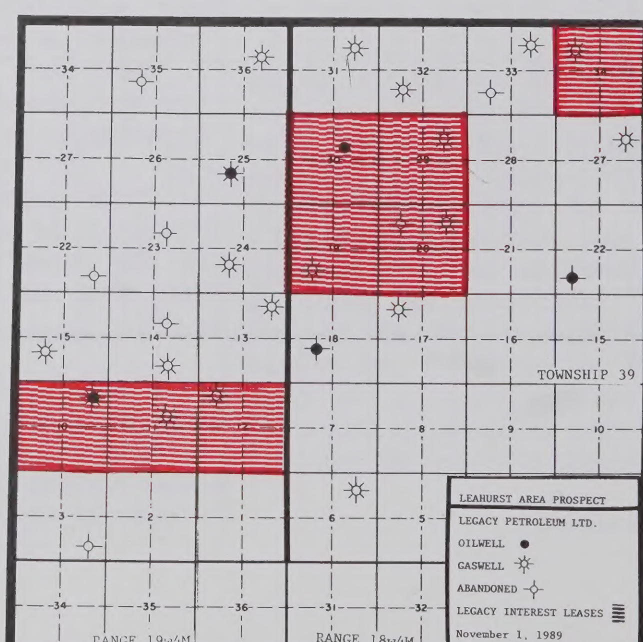
Your Company's holdings in the Halkirk North area are highlighted on the page four map and reserves are noted on page seven.

### *Leahurst, Alberta*

Perhaps one of the most notable events of the current fiscal year was the acquisition of properties in the Leahurst area, in close proximity to your Company's Halkirk/Castor properties. A total of eight wells located on an eight section spread highlighted below were acquired for a cash consideration of $40,000. Of the eight wells acquired, one is a pumping oilwell with solution gas, two are producing gas wells and five are currently shut-in. Your Company's interest in this area ranges from 15% to 78.5% and is the operator.

As noted in the Reserves Report on page seven your Company's interest of proved producing and non-producing for Leahurst totals 1,003 MMCF of natural gas and equivalent oil with an additional 602 MMCF of probable reserves. Undiscounted present worth of the newly acquired properties is over $3,000,000.00 according to the engineering report prepared for your Company as of 01 August 1989.

The producing gaswells are being produced at maximum under contract to TransCanada Pipelines Ltd. Your Company is currently evaluating the shut-in gaswells with a view to bringing same on production at a minimal cost.



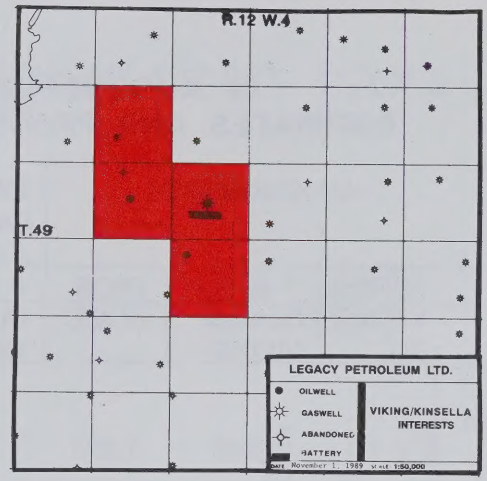
***Viking-Kinsella, Alberta***

Production revenue from the Viking Kinsella Prospect was hampered during the fiscal year due to problems with the operator of the solution gas facility. Unfortunately, these problems were not resolved until April of this year and therefore there was little or no production from this prospect during the current fiscal year. The properties did go back on production for the months of May and June prior to the standard summer shut-down. The battery has now been placed back on production and is expected to produce until the summer of 1990.

In July of this year, your Company sold a 50% working interest in the four section prospect for a cash consideration of $125,000. Funds from this sale will be used to reduce bank debt, redeem First Preferred Shares issued to purchase said properties, and to further enhance production at Viking. The sale of working interest will leave your Company with a 50% working interest in 13-16-49-12 W4M and 11-20-49-12 W4M. With regard to production from 6-21-49-12 W4M your Company is negotiating the purchase of 50% interest from Signalta Resources Ltd., which would after the sale referenced above, still leave your Company with a 50% interest in the well and battery in 6-21-49-12 W4M.

During the summer your Company plugged off the Basal Quartz zone in 6-21-49-12 W4M and perforated the Wabamun (D1) zone. According to the 01 August 1989 engineering report remaining recoverable sales gas is estimated at 825 MMCF. Your Company is currently negotiating a sales contract for the gas from this zone and the well is expected to be placed on production 01 November 1989. Your Company has a 50% working interest in gas production from the Wabamun zone.

During the balance of the year, your Company will endeavour to enhance production from the Viking-Kinsella prospect; however the lack of production during the fiscal year under review severely hampered cash flow. Fiscal 1990 should reflect ten months production from this prospect.




***Steelman, Saskatchewan***

During the past fiscal year very little activity took place in the Steelman prospect of southeastern Saskatchewan. No additional drilling was undertaken and it would appear that the well operated by COHO in 1988 in LSD 15, Section 36, Township 5, Range 6 W2M will be converted to a water disposal well.

Your Company currently receives working interest revenue from 5-36-5-6 W2M and royalty revenue from wells in 11-36-5-6 W2M and 13-36-5-6 W2M. Efforts to continue the northeast quarter of Section 25, Township 5, Range 6 W2M were unsuccessful, leaving your Company with varying interests in one section in this area.

**UNITED STATES**

There are no new developments to report on your Company's gross overriding royalty acreage in the State of Montana. Activity continues to be depressed in the Northern States and your management does not anticipate any significant changes prior to the end of fiscal 1990.

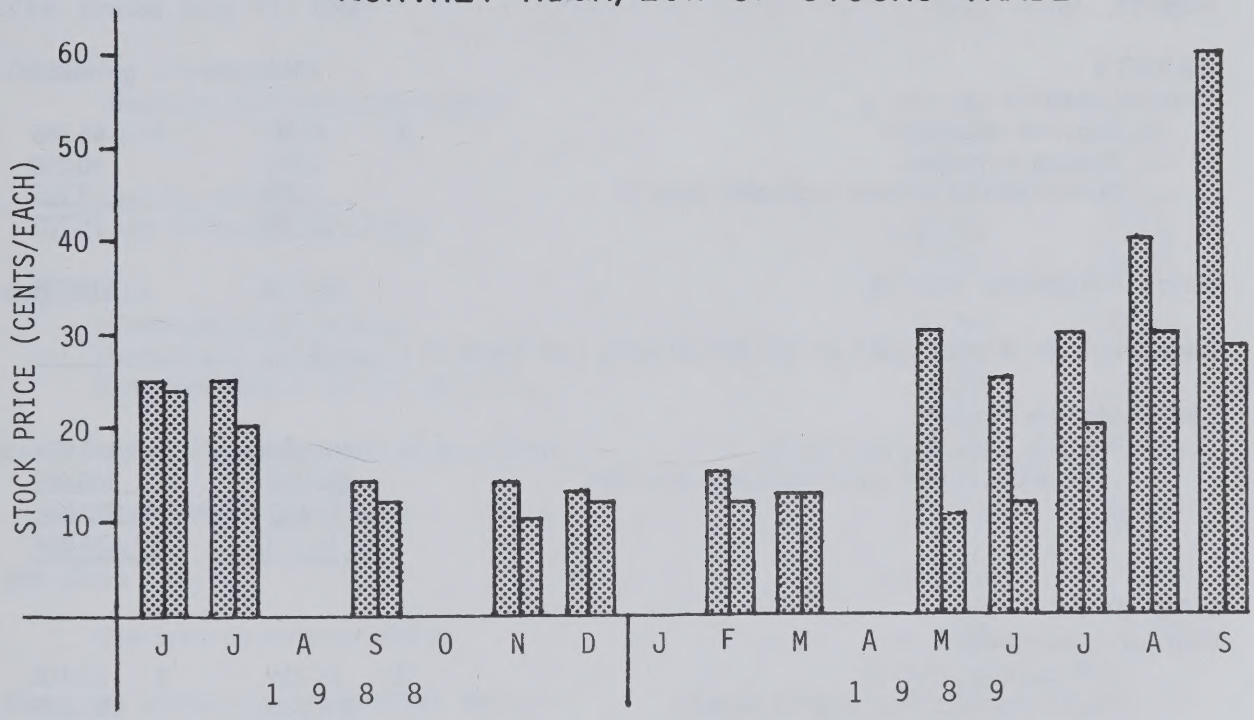
We continue to seek out companies that may be interested in acquiring the substantial tax loss of the U.S. subsidiary. This tax loss expires in 2005.

# 01 AUGUST 1989 RESERVES REPORT
# ESTIMATES AND PRESENT WORTH OF PIPELINE GAS

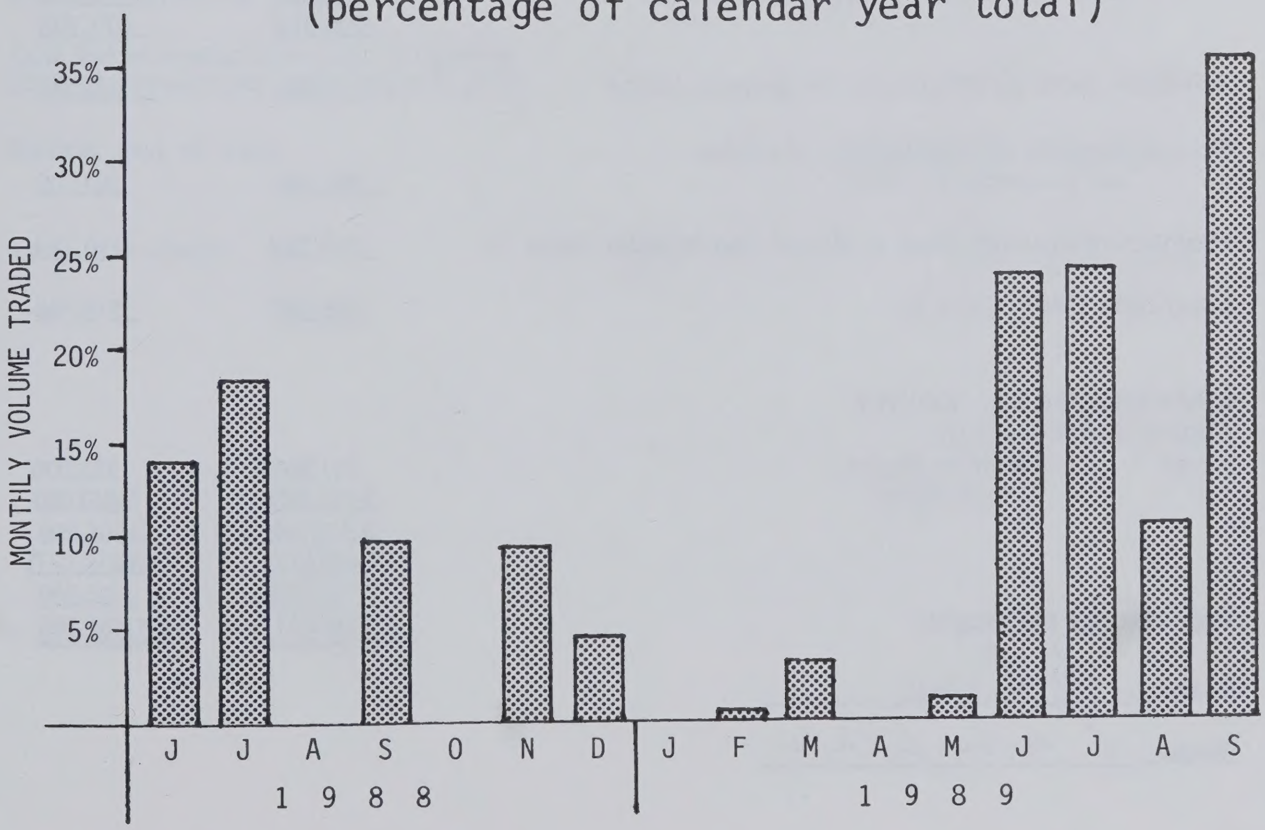
| FIELD: | HALKIRK NORTH | | | HALKIRK EAST (CASTOR) | LEAHURST | | | VIKING-KINSELLA |
|---|---|---|---|---|---|---|---|---|
| POOL: | PPROD | P NON-P | PROB | P NON-P | PPROD | P NON-P | PROB | PPROD |
| | VIKING/ BQ | GLAUC/ VIKING | GLAUC | GLAUC/ VIKING | BQ/ GLAUC | VIKING/ BQ/ GLAUC | BQ/ VIKING | WABAMUN/ SPARKY 'C' |
| Original Gas in Place MMCF | ( 1 ) | 3,655 | 1,973 | ( 1 ) | 5,224 | 3,352 | 3,371 | ( 1 ) |
| Rec. Factor | | 65% | 25% | | Var. | Var. | Var. | |
| Ult. Rec. Raw Gas MMCF | 2,788 | 2,375 | 493 | 1,260 | 2,919 | 1,736 | 1,779 | 1,371 |
| Cum. Prod. to 01 Aug 89 MMCF | 1,671 | - | - | 697 | 271 | - | - | 157 |
| Surface Loss | 10% | Var. | 10% | 5% | 5% | Var. | Var. | 5% |
| Remaining Reserves MMCF | 1,005 | 2,192 | 444 | 535 | 2,516 | 1,622 | 1,621 | 1,154 |
| Company Interest MMCF | 828 | 362 | 77 | 261 | 378 | 625 | 717 | 525 |
| Burdens | Var. | FR 12.5% | FR 12.5% | CR/FR + Var. | NCR + 10 | CR/FR + Var. | CR/FR + Var. | CR/FR + Var. |
| Net Company Interest MMCF | 721 | 317 | 69 | 186 | 261 | 481 | 602 | 410 |
| Present Worth $000' s | | | | | | | | |
| 0% | 1,187 | 554 | 183 | 109 | 729 | 1,079 | 4,019 | 963 |
| 15% | 536 | 273 | 46 | 73 | 263 | 450 | 343 | 453 |
| 20% | 450 | 231 | 33 | 65 | 211 | 358 | 218 | 381 |

(1) Decline curve analysis.
PPROD is Proven Producing      P NON-P is Proven Non-Producing      PROB is Probable Additional

MONTHLY HIGH/LOW OF STOCKS TRADED




MONTHLY VOLUME OF STOCKS TRADED
(percentage of calendar year total)



# CONSOLIDATED BALANCE SHEET

**May 31, 1989**

| | 1989 | 1988 |
|---|---|---|
| **ASSETS** | | |
| ***Current Assets*** | | |
| Accounts receivable | $ 41,001 | $ 64,365 |
| Prepaid expenses | 9,577 | 10,280 |
| Current portion of notes receivable (Note 2) | 2,125 | 2,125 |
| | 52,703 | 76,770 |
| ***Notes Receivable*** (Note 2) | 511,519 | 513,644 |
| ***Investment in & Advances to 363304 Alberta Ltd.*** (Note 3) | 48,563 | --- |
| ***Capital Assets*** (Note 4) | | |
| Property, plant and equipment | 1,344,682 | 1,010,294 |
| Less: accumulated depreciation and depletion | 243,056 | 166,440 |
| | 1,101,626 | 843,854 |
| | $ 1,714,411 | $ 1,434,268 |
| **LIABILITIES** | | |
| ***Current Liabilities*** | | |
| Bank overdraft(Note 5) | $ 53,754 | $ 34,476 |
| Accounts payable and accrued liabilities | 337,663 | 101,323 |
| Salary payable | 46,048 | 29,004 |
| Due to shareholders (Note 6) | 1,769 | 3,907 |
| Current portion of long-term debt (Note 8) | 166,680 | 103,083 |
| | 605,914 | 271,793 |
| ***Advance from Landlord on Long-term Lease*** | 3,375 | 6,375 |
| ***Bonus payable to Officer and Director*** | | |
| Due December 31, 1995 | 391,000 | 391,000 |
| ***Promissory Notes Payable to Officer and Director*** (Note 7) | 210,784 | 210,784 |
| ***Long-term Debt*** (Note 8) | 420,686 | 218,324 |
| **SHAREHOLDERS' EQUITY** | | |
| ***Capital Stock*** (Note 9) | | |
| Issued - Preferred shares | 111,500 | 112,000 |
| Class A shares | 3,434,069 | 3,443,069 |
| | 3,545,569 | 3,555,069 |
| | (3,462,917) | (3,219,077) |
| | 82,652 | 335,992 |
| | $ 1,714,411 | $ 1,434,268 |

**Approved by the Board:**

Director: M. Hwang

Director: L. Monfelandi

## CONSOLIDATED STATEMENT OF LOSS AND DEFICIT

| Year Ended May 31, 1989 | 1989 | 1988 |
|---|---|---|
| ***Operating Income*** | | |
| Petroleum and natural gas revenue | $ 314,465 | $ 261,926 |
| Other | 16,420 | 52,422 |
| | 330,885 | 314,348 |
| Less: Royalties | 34,499 | 28,841 |
| Less: Production expenses | 223,395 | 170,296 |
| | 72,991 | 115,211 |
| ***Expenses*** | | |
| Interest on long-term debt | 55,156 | 32,861 |
| General and administrative | 167,100 | 152,850 |
| Investment loss in 363304 Alberta Ltd. | 15,925 | --- |
| | 238,181 | 185,711 |
| ***Loss before Depletion and Depreciation*** | ( 165,190) | ( 70,500) |
| Depletion and depreciation | 76,616 | 64,858 |
| ***Net Loss*** | ( 241,806) | ( 135,358) |
| Dividends on preferred shares | 8,710 | 10,820 |
| ***Net Loss attributed to common shares*** | ( 250,516) | ( 146,178) |
| **Deficit, beginning of year** | (3,219,077) | (3,082,939) |
| Cost below average issue price of common shares purchased and cancelled (Note 9(a)) | 6,676 | 10,040 |
| **Deficit, end of year** | $(3,462,917) | $(3,219,077) |
| ***Loss per Share*** | $ (0.07) | $ (0.03) |

## CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

**Year Ended May 31, 1989**

| | 1989 | 1988 |
|---|---|---|
| ***Operations*** | | |
| Net Loss | $( 241,806) | $( 135,358) |
| Add: Depletion and depreciation | 76,616 | 64,858 |
| Investment loss in 363304 Alberta Ltd. | 15,925 | --- |
| Loss (Gain) on sale of capital assets | --- | ( 162) |
| | ( 149,265) | ( 70,662) |
| Change in working capital other than cash | 272,313 | 33,025 |
| | 123,048 | ( 37,637) |
| ***Financing*** | | |
| Issue of preferred shares on acquisition of property and equipment | 92,500 | 32,000 |
| Issue of common shares on acquisition of property and equipment | --- | 32,480 |
| Proceeds on sale of capital assets | --- | 114,180 |
| Proceeds on note receivable | 2,125 | 2,125 |
| Increase in long-term debt, net of repayment | 265,959 | 71,221 |
| Redemption of preferred shares | ( 93,000) | ( 90,000) |
| Dividend on preferred shares | ( 8,710) | ( 10,820) |
| Common Shares returned to Treasury | ( 2,324) | ( 3,460) |
| | 256,550 | 147,726 |
| | 379,598 | 110,089 |
| ***Investing*** | | |
| Additions to capital assets | ( 334,388) | ( 205,272) |
| Advances to 363304 Alberta Ltd. | ( 64,488) | --- |
| | ( 398,876) | ( 205,272) |
| ***Increase (Decrease) in Cash*** | ( 19,278) | ( 95,183) |
| ***Cash (Deficiency), beginning of year*** | ( 34,476) | 60,707 |
| ***Cash (Deficiency), end of year*** | $ ( 53,754) | $( 34,476) |

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
**Year Ended May 31, 1989**

## 1. SUMMARY OF ACCOUNTING POLICIES

### (a) *Principles of Consolidation*

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Harkor Developments Ltd. and Legacy Oil and Gas. Ltd. and its wholly-owned United States subsidiaries, Legacy Oil and Gas Inc. and Benchlands Oil and Gas Inc.

### (b) *Capital Assets*

i) *Petroleum and Natural Gas Properties*

The Company follows the full cost method of accounting for oil and gas operations whereby all costs related to exploration and development of oil and gas reserves are capitalized. Capitalized costs include those related to lease acquisitions, geological and geophysical activities, carrying costs on non-producing property, drilling of wells and applicable overhead expenses. General and administrative expenses totalling $29,900 were capitalized for the year. These capitalized costs are accumulated in separate geographically located cost centers for each country in which the Company operates, at present Canada and the United States.

ii) *Depletion and Depreciation*

Depletion of oil and gas properties and depreciation of production equipment and facilities are calculated on the unit-of-production method based upon:
- total estimated proven producing and non-producing reserves, before royalty, as determined by independent engineers,
- total capitalized costs plus provision for future costs in developing proved reserves as determined by independent engineers,
- relative volumes of oil and gas reserves and production converted at a ratio of one barrel of oil to six thousand cubic feet of gas.

Other capital assets are depreciated on a declining balance method at annual rates of 20% to 30%.

iii) *Ceiling test*

The carrying amount of property, plant and equipment is limited to the sum of:
- estimated future net revenues from proven reserves as determined by independent engineers, less future production-related general and administrative and interest expenses, applicable income tax and preferred share dividends, plus
- the cost less impairment of undeveloped properties.

The calculation of future net revenues is based upon sales prices and costs, and the Income Tax and Alberta Royalty Tax Credit legislation in effect at the end of the fiscal year. No write-down of the carrying amount was required in the year.

(c) ***Joint Ventures***

Substantially all of the Company's exploration and production activities are conducted jointly with others and, accordingly, the accounts reflect only the Company's proportionate interest in such activities.

(d) ***Foreign Currency Translation***

The foreign subsidiaries accounts have been translated into Canadian dollars at the rate in effect at the balance sheet date for monetary assets and liabilities. Non-monetary assets and liabilities are translated at applicable historical rates. Revenue and expense items are translated at the average rate of exchange for the year.

(e) ***Advance from Landlord on Long-term Lease***

This advance is being applied against monthly rent of office premises, over the term of the lease.

(f) ***Comparative Figures***

Certain of the comparative figures have been reclassified to confirm to the current year's presentation.

(g) ***Working Capital Deficiency***

The Company incurred a loss in fiscal 1988 and 1989 and at 31 May 1989 had a working capital deficiency. Continued operations may be dependent on future events including maintaining current (September 1989) gas prices and reduction in operating, general and administrative expenses. Management expects cash flow to increase by achieving consistent production through the fiscal year. In the opinion of management, the working capital deficiency will be eliminated.

## 2. NOTES RECEIVABLE

| | 1989 | 1988 |
|---|---|---|
| Notes receivable due December 31, 1995 | $ 391,000 | $ 391,000 |
| Notes receivable due October 1990, repayable in annual installments of $1,525 to May 31, 1990 with the balance of $94,751 due; $68,181 July 1, 1990 and $26,570 October 1990. | 96,275 | 97,800 |
| Notes receivable due December 1995, repayable in annual installments of $600 to May 31, 1994 with the balance of $23,368 due; $11,668 June 1994 and $11,700 December 1995. | 26,369 | 26,969 |
| | 513,644 | 515,769 |
| Current Portion | 2,125 | 2,125 |
| | $ 511,519 | $ 513,644 |

The notes receivable are non-interest bearing and are due from present and former officers and directors of the Company.

3. **INVESTMENT IN AND ADVANCES TO 363304 ALBERTA LTD.**

On 01 December 1988 the Company acquired a 71.07% interest in the issued shares of 363304 Alberta Ltd. No cash consideration was given. The net assets acquired are summarized below.

| | |
|---|---|
| Properties and equipment | $ 58,381 |
| Less liabilities | 72,065 |
| | (13,684) |
| Less minority interests | 3,959 |
| Deficiency in underlying net book value of assets | $ ( 9,725) |

363304 Alberta Ltd. has sustained continued losses in operating since date of acquisition. Therefore the acquisition has been accounted for by the equity method.

At 31 May 1989 the investment in and advances to 363304 Alberta Ltd. consisted of the following:

| | |
|---|---|
| Advances to 363304 Alberta Ltd. | $ 64,488 |
| Investment loss | (15,925) |
| | $ 48,563 |

4. **CAPITAL ASSETS**

| | 1989 | | | 1988 |
|---|---|---|---|---|
| | Cost | Accumulated Depletion and Depreciation | Net Book Value | Net Book Value |
| Canadian petroleum and natural gas properties | $ 1,122,579 | $ 154,928 | $ 967,651 | $ 724,557 |
| Automotive | 49,997 | 11,038 | 38,959 | 13,596 |
| Office equipment | 33,664 | 18,531 | 15,133 | 18,866 |
| Plant and wellsite equipment | 138,442 | 58,559 | 79,883 | 86,835 |
| | $1,344,682 | $ 243,056 | $ 1,101,626 | $ 843,854 |

5. **BANK OVERDRAFT**

The bank overdraft is secured with a $1,000,000 demand debenture providing fixed charge on specific properties and floating charge on other assets.

6. **DUE TO SHAREHOLDERS**

The amounts due to shareholders are unsecured, are either non-interest bearing or bear interest at a rate of 15% and are due on demand.

7. **PROMISSORY NOTES PAYABLE TO OFFICER AND DIRECTOR**

| | 1989 | 1988 |
|---|---|---|
| Promissory note, payable to A.K. Mossfeldt due April 1, 1995 | $ 39,250 | $ 39,250 |
| Promissory note, payable to A.K. Mossfeldt due April 1, 1995 | 171,534 | 171,534 |
| | $ 210,784 | $ 210,784 |

## 8. LONG-TERM DEBT

| | 1989 | 1988 |
|---|---|---|
| U.S. Bank Demand Loan (US $48,058) bearing interest at 14% per annum secured with assets of the President of the Company | $ 59,111 | $ 66,497 |
| Finance contracts bearing interest at the weighted average of 13.% per annum repayable in monthly installments of $1241 principal and interest due 1992 and 1993. Secured with automobile equipment | 42,150 | 14,270 |
| Bank loan bearing interest at prime plus 2.5% repayable in monthly installments of $500 principal and interest due July 1989 secured with assets of the President of the Company | 1,804 | 7,035 |
| Alberta Small Business Loan bearing interest at 9.0% per annum repayable in monthly installments of $1900 principal and interest due 15 May 1997 | 129,755 | 139,443 |
| Bank term loans bearing interest at prime plus 1.5% repayable in monthly installments of $6,467 principal plus interest due 1994 | 354,546 | 94,162 |
| | 587,366 | 321,407 |
| Less portion due within one year | 166,680 | 103,083 |
| | $420,686 | $218,324 |

The Alberta Small Business Loan and bank term loans are secured with:

(a) General assignment of book debts.
(b) Specific assignment of TransCanada Pipelines Gas contract.
(d) Demand debenture for $1,000,000 providing fixed charge on specific properties and floating charge on all other assets.

Repayment of long-term debt over the next five fiscal years will be as follows:

| | |
|---|---|
| 1990 | $166,680 |
| 1991 | 103,016 |
| 1992 | 104,208 |
| 1993 | 100,092 |
| 1994 | 57,599 |
| Subsequent | 55,771 |
| | $587,366 |

## 9. CAPITAL STOCK

**Authorized:**

Unlimited Class "A" voting common shares
Unlimited Class "B" non-voting common shares
500,000 Preferred Shares

**Issued:**

(a) ***Class A Voting Shares***

| | 1989 | |
|---|---|---|
| | Number of Shares | Stated Value |
| Balance, beginning of year | 3,442,958 | $ 3,443,069 |
| Purchased for cash and cancelled | ( 9,000) | ( 9,000) |
| | 3,433,958 | $ 3,434,069 |

The excess of the average carrying value of common shares at the purchase date over the purchase consideration has been charged to retained earnings (deficit).

(b) ***First Preferred Shares***

| | 1989 | |
|---|---|---|
| | Number of Shares | Stated Value |
| Balance, beginning of year | 22,090 | $112,000 |
| Issued | 19 | 92,500 |
| Redeemed | ( 3,090) | ( 93,000) |
| | 19,019 | $111,500 |

The shares have been designated as follows:

i) 8% cumulative, redeemable, retractable, convertible

ii) the shares are retractable as follows:

19000 shares at $19,000 on 01 October 1989
9.5 shares at $46,250 on 01 December 1989
9.5 shares at $46,250 on 01 June 1990

iii) in the event of default, provisions exist to convert the shares to common trading shares.

(c) ***Stock Options***

The company has entered into an option agreement with certain directors and employees whereby 550,000 Class A common shares were reserved for issue at an exercise price of $0.11 per share. The agreement expires April 30, 1996.

## 10. REMUNERATION OF DIRECTORS AND SENIOR OFFICERS

Remuneration provided in the books to directors and senior officers was $89,004 of which $46,048 remains unpaid.

## 11. INCOME TAXES

The Company has accumulated losses for Canadian income tax purposes of $647,313 and $663,201 (U.S.) for United States income tax purposes, the related benefit of which has not been recognized in the financial statements. Unless sufficient taxable income is earned by the Company, the losses for Canadian income tax purposes expire as follows:

| | |
|---|---|
| 1990 | $ 43,909 |
| 1991 | 381,139 |
| 1992 | 10,401 |
| 1993 | 2,119 |
| 1995 | 32,687 |
| 1996 | 177,058 |

The losses for United States income tax purposes will expire in 2005.

## 12. SUBSEQUENT EVENTS

On 01 July 1989 the Company sold a 50% working interest in a petroleum and natural gas property referred to as Viking Kinsella Prospect for a cash consideration of $125,000.

In September 1989 the Company obtained an additional bank loan in the amount of $147,000 to convert the bank overdraft to a term loan. The loan is secured with the $1,000,000 demand debenture referred to in Note 8.

## 13. SEGMENTED INFORMATION

The Company's operations are conducted in Canada and the United States in petroleum and natural gas production. Substantially, all of the Company's activities during the year were in Canada.

*M. Jane McKinnon*
*Chartered Accountant*

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933 - 17th AVENUE S.W.
CALGARY, ALBERTA T2T 5R6

TELEPHONE (403) 244-2840

**To the Shareholders of
Legacy Petroleum Ltd.:**

I have examined the consolidated balance sheet of Legacy Petroleum Ltd. as at May 31, 1989 and the consolidated statements of loss, deficit and changes in financial position for the year then ended. My examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as I considered necessary in the circumstances.

In my opinion, these consolidated financial statements present fairly the financial position of the Company as at May 31, 1989 and the results of its operations and the changes in its financial position for the year ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

M. Jane McKinnon

15 September 1989
Calgary, Alberta

M. Jane McKinnon
Chartered Accountant

## CORPORATE HISTORY

Legacy Petroleum Ltd. was incorporated October 14, 1970 as Francis Creek Mines Ltd.(NPL), a private Company. On June 14, 1971 Francis Creek Mines Ltd. (NPL) changed its name to Frances Creek Mines Ltd. (NPL), a private Company. On December 21, 1971, Frances Creek Mines Ltd. (NPL) became a publicly listed Company on the Alberta Stock Exchange. In September 1975, the Company changed its name to Cal-West Petroleums Ltd. (NPL). In April 1976 the Company acquired all the issued and outstanding shares of Harkor Developments Ltd. whose primary asset was a gold mining claim at Granite Creek, British Columbia.

In February 1983 Cal-West was continued under the Alberta Business Corporations Act. In March of that year, control of the Corporation was obtained by a group of businessmen headed by A. Kenneth Mossfeldt, President of Legacy Oil and Gas Ltd. In September 1983 shareholders of both Cal-West and Legacy approved a share exchange whereby Cal-West acquired the 3,300,009 issued and outstanding shares of Legacy for a like number of shares of Cal-West.

In May of 1986 shareholders ratified a change of name from Cal-West Petroleums Ltd. (NPL) to Legacy Petroleum Ltd.; approved a consolidation of share capital based on five (5) of the old Cal-West shares for each one (1) of the new Legacy shares; and approved the creation of a Class "B" non-voting common share and the creation of Preferred Shares. No Class "B" shares have been issued to date.

The Cal-West designation for the Corporation was delisted from the Alberta Stock Exchange and "Legacy Petroleum Ltd." was called for trading on June 26, 1985. The initial trade was made on August 21, 1985 at 35 cents per share.

In 1985 Legacy made its first operating acquisition of Alberta producing properties from North Canadian Oils Limited, formerly Merland Explorations Ltd., at Halkirk, Alberta for $250,000.00 of First Preferred Shares. Legacy completed the redemption of these shares 01 November 1988.

In September 1986 the Corporation increased its Alberta holdings with the addition of producing properties and processing facilities at Castor, Alberta. This acquisition, at a cost of $135,000.00, was paid for with 225,000 Class "A" common trading shares from Treasury. The addition of these properties gave the Corporation a substantial exposure in this gas prolific area of southeast Alberta.

In mid 1988 the opportunity to purchase a substantial working interest in an oil battery and additional properties in the Viking-Kinsella area of Alberta arose. The Corporation successfully negotiated this acquisition from North Canadian Oils Limited at a cost of $92,500.00 in First Preferred Shares, redeemable over a two-year period.

In the spring of 1989 the Corporation again increased its holdings and production in the Stettler area with the acquisition of additional production and undeveloped properties at Leahurst from Paloma Petroleum Ltd. for a cash consideration of $40,000.00.

Since September 1986 the Corporation has acquired additional interests in the Castor properties from other joint venture participants, the most notable being the acquisition of all of Canadian Occidental's interests for a cash consideration of $12,500.00. As well, the Corporation successfully negotiated a conclusion to the litigation involving the Castor properties and its previous owner/operator Pangaea Petroleum Limited.

Legacy

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Legacy Petroleum Ltd.